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# REGULATORY CONTROLS ON LARGE LAW FIRMS: A COMPARATIVE PERSPECTIVE

Geoffrey C. Hazard, Jr.\* & Ted Schneyer\*\*

## Introduction

For nearly two centuries, the vast majority of lawyers in private practice in the United States practiced alone or in firms with no more than two or three colleagues. Since 1950, however, and especially in the last quarter-century, practice in much larger firms has become so common that the large firm is to a considerable degree displacing the traditional practice settings.<sup>1</sup> While this trend has been most pronounced in the United States, it is not uniquely American. Large firms have also become salient in international law practice as well as in domestic practice in Western Europe and much of the common law world.

Just as lawyers practice in various settings, so they can be regulated by various means. The lawyer's incentive to maintain a good reputation has long served as an informal control. The more formal controls that society has chiefly relied on to date also evolved when solo and small-firm practice were the norm. One such mechanism is the bar-administered disciplinary process, which bears a striking resemblance to the controls that medieval guilds exercised over local practitioners of a craft.<sup>2</sup> In the disciplinary process, a lawyer is charged with misconduct; investigations and hearings determine whether the lawyer violated professional norms; and sanctions such as reprimand, suspension, or disbarment

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1. According to a recent bar association report, "The more than 105,000 lawyers in the 700 largest law firms are the most prominent sector of the profession [in the United States] today. . . . [T]he emergence of what came to be referred to as the 'Wall Street law firms' has profoundly affected the structure and operation of many law firms [and the bar] generally." N. Y. STATE BAR ASS'N, PRESERVING THE CORE VALUES OF THE AMERICAN LEGAL PROFESSION (April 2000), *quoted in* ANDREW L. KAUFMAN & DAVID B. WILKINS, PROBLEMS IN PROFESSIONAL RESPONSIBILITY FOR A CHANGING PROFESSION 757, 758 (4th ed. 2002).

2. See ELLIOTT A. KRAUSE, DEATH OF THE GUILDS: PROFESSIONS, STATES, AND THE ADVANCE OF CAPITALISM, 1930 TO THE PRESENT 2-5 (1996) (describing how guilds regulated the conduct of those engaged in a craft).

are imposed on violators.<sup>3</sup> Other traditional mechanisms center on the exercise of judicial authority. Courts have long entertained civil claims against lawyers for malpractice. In those cases, clients seek compensation for losses caused by their lawyers' breach of fiduciary duties or prevailing standards of care. Courts have also exerted direct control over lawyers appearing before them on behalf of litigants, by disqualifying those who are embroiled in conflicts of interest, for example, or by sanctioning lawyers for procedural violations or contempt.

This Article considers how well these traditional controls, formal and informal, can be expected to regulate large-firm practice, and whether practice in that form calls for a distinctive mix of regulatory techniques. We explore these issues by comparing the structure, clientele, services, and characteristic ethical problems of large firms with the corresponding features of solo and small-firm practice. The Article concludes that disciplinary controls, which in many countries remain under-developed, are especially unlikely to constrain lawyers in large firms. Civil liability and disqualification have greater promise, but internal monitoring and sanctioning by large firms motivated to protect their institutional interests and reputations must also play a major role.<sup>4</sup>

### Traditional Forms of Private Practice

The practice of law became identifiable as a vocation in Western Europe by around 1600.<sup>5</sup> During the ensuing centuries, government increasingly promulgated rules—the lawyer's stock-in-trade—to structure economic and social activities. Business, once conducted almost exclusively by sole proprietorships and family partnerships, was increasingly conducted by multi-party associations, joint stock companies, and, eventually, corporations. These more complex business forms required technically precise legal documents and spawned more litigation than the older forms. Demand for legal services rose accordingly. By 1800, substantial legal professions existed in England, France, Germany, Italy, and the United States. Skilled practitioners could be found elsewhere as well.<sup>6</sup>

Until the late nineteenth century, lawyers everywhere remained enterprises unto themselves. Though often assisted by apprentices, they were typically solo practitioners who attained most of their knowledge and skill on the

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3. In the United States, however, the organized bar has had to share disciplinary authority with the courts, which oversee the disciplinary process. See Theodore J. Schneyer, *The Incoherence of the Unified Bar Concept: Generalizing from the Wisconsin Case*, 1983 AM. B. FOUND. RES. J. 17–24, 47 (discussing the subordination of the bar's authority to judicial control).

4. Internal controls in law firms are not "regulation" in the strict sense, but, like public regulation, they are designed to constrain the conduct of the lawyers in those firms.

5. See LAWYERS IN EARLY MODERN EUROPE AND AMERICA 11 (Wilfred Prest ed., 1981).

6. *Id.* at 181–204; see generally LAWRENCE M. FRIEDMAN, A HISTORY OF AMERICAN LAW 266–67 (1973); LAWYERS AND THE RISE OF WESTERN POLITICAL LIBERALISM: EUROPE AND NORTH AMERICA FROM THE EIGHTEENTH TO TWENTIETH CENTURIES (Terence C. Halliday & Lucien Karpak eds., 1997); Gino Gorla & Luigi Moccia, *A "Revisiting" of the Comparison Between "Continental Law" and "English Law" (16th to 19th Century)*, 2 J. LEGAL HIST. 143 (1981).

job.<sup>7</sup> Most had a general practice. They created and interpreted legal documents such as deeds, mortgages, contracts, leases, and wills. They also represented parties in legal disputes, chiefly over rights in real estate. In some places, courtroom advocacy and "office practice" evolved as distinct occupations,<sup>8</sup> but further specialization was rare. Most clients were individuals who resided in their lawyer's community.

This "solo/local" practice pattern still prevails outside Western Europe and the common law world, although two- and three-lawyer firms have often emerged as additional service providers. Where the pattern no longer prevails, it remains a non-trivial aspect of practice.

### Traditional Control Mechanisms

In a traditional, solo/local practice environment, professional norms are mostly defined by local custom and are informally enforced. In that environment, practice requires continual interaction with a small, stable group of local lawyers and court officials. Their refusal to cooperate with a lawyer who is inept, obnoxious, or unreliable can be a powerful sanction; it is hard to maintain a local practice in the face of a professional boycott. Traditional practice also requires a continual inflow of new engagements, many of them generated by referrals. As a result, the viability of one's practice depends heavily on maintaining a good reputation with local lawyers and clients. The best way to maintain a good reputation is to behave well.

Even where the solo/local pattern prevails, however, these informal controls are usually supplemented by a disciplinary process and the forms of judicial oversight noted above. But their role is modest. The frequent weakness of

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7. Abraham Lincoln was representative of his era in learning law through an apprenticeship. ALBERT A. WOLDMAN, *LAWYER LINCOLN* 11-24 (1994). But lawyers from wealthy families here and abroad often received an introduction to law at universities. See, e.g., 2 ANTON-HERMANN CHROUST, *THE RISE OF THE LEGAL PROFESSION IN AMERICA* ch. 4 (1965); FRIEDMAN, *supra* note 6, at 281; see also WILLIAM P. LAPIANA, *LOGIC AND EXPERIENCE: THE ORIGIN OF MODERN AMERICAN LEGAL EDUCATION* (1994) (describing the origins and early influence of Harvard Law School).

8. In England, for example, barristers represented clients in court, while solicitors drafted documents and gave advice on family, property, and business matters. On the development and traditional regulation of the legal profession(s) in England, see WILLIAM H. HURLBURT, *THE SELF-REGULATION OF THE LEGAL PROFESSION IN CANADA AND IN ENGLAND AND WALES* (2000). On comparable developments in France, see JOHN LEUBSDORF, *MAN IN HIS ORIGINAL DIGNITY: LEGAL ETHICS IN FRANCE* chs. 1-4 (2001). On the very early structure and regulation of the English bar, see Jonathan Rose, *The Legal Profession in Medieval England: A History of Regulation*, 48 SYRACUSE L. REV. 1, 49-63 (1998). English barristers have traditionally been barred from forming partnerships, but permitted to share chambers. W.W. Boulton, *The Legal Profession in England: Its Organization, History and Problems*, 43 A.B.A. J. 507, 507 (1957). Advocates in France and certain other civil law countries have faced the same constraint, on the theory that each advocate must be free to decide how a client's affairs should be handled. JOHN HENRY MERRYMAN, *THE CIVIL LAW TRADITION* 113 (1969). On the gradual reconciliation of modern pressures to form law firms with the French *avocat's* duty not to subordinate his judgment to that of other *avocats*, see LEUBSDORF, *supra*.

the organized bar,<sup>9</sup> the reluctance of lawyers to fund a regulatory system from which they reap no significant personal benefit, and the sense (among lawyers, at least) that informal controls are adequate have limited the development and use of the disciplinary process.<sup>10</sup> Judges have traditionally sanctioned lawyers directly only for litigation-related misconduct, which in solo/local practice environments is infrequent.<sup>11</sup> Malpractice suits against a local lawyer by a local client represented by another local lawyer have traditionally been rare, too.

Because little more than anecdotal evidence exists on the point, reasonable people may differ about the effectiveness of these formal and informal controls in solo/local practice environments. But, however effective they may be in those environments, there are good reasons to expect some of them to be relatively ineffective in regulating practice in today's large law firms.

### Fast Forward to the Late Twentieth Century

While the vast majority of American lawyers continued to practice as solos or in very small firms until the 1950s,<sup>12</sup> the traditional pattern held even greater sway abroad. Until quite recently, firms with more than a handful of lawyers remained uncommon in England and virtually non-existent on the Continent and in Latin America, India, and Japan. The large law firm is an American invention and export.

Around 1900, as new forms of business regulation took shape, prototypes of today's largest firms sprang up in New York City and other business centers. By the 1970s, a strong trend toward large-firm practice was evident. While only thirty-eight American law firms had more than fifty lawyers in the late 1950s, by 1986 over 500 firms were that large and about half of them had more than 100 lawyers.<sup>13</sup> By the 1990s, as a result of internal growth and mergers, the largest 100

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9. See, e.g., JAMES WILLARD HURST, *THE GROWTH OF AMERICAN LAW: THE LAW MAKERS* 285-89 (1950) (discussing the ineffectiveness and weak organization of the bar in the United States during most of the nineteenth century).

10. On the evolution of the rules of professional conduct that serve as the basis for discipline in the United States, see Geoffrey C. Hazard, Jr., *The Future of Legal Ethics*, 100 YALE L.J. 1239, 1249-55 (1991).

11. On the reluctance of courts to police lawyers outside the realm of litigation, see Susan P. Koniak, *The Law Between the Bar and the State*, 70 N.C. L. REV. 1389, 1461-78 (1992).

12. Indeed, as late as 1951, nearly 60% of the lawyers practicing in the United States were solo practitioners. AM. BAR FOUND., *THE 1971 LAWYER STATISTICAL REPORT* 10 (1972). By 1989, however, more private practitioners were working in firms than as solos. RICHARD L. ABEL, *AMERICAN LAWYERS* 179, 300 (1989).

13. Marc Galanter & Thomas M. Palay, *Why the Big Get Bigger: The Promotion-to-Partner Tournament and the Growth of Large Law Firms*, 76 VA. L. REV. 747, 749 (1990). Whether new technological developments, such as the capacity to conduct legal research by computer, will trigger a significant counter-trend toward solo and small-firm practice remains to be seen.

law firms accounted for 20% of all legal fees.<sup>14</sup> Several firms now have over 1,000 lawyers.

### Large-Firm Practice Compared with Solo and Small-Firm Practice

One can assess the prospects for effectively regulating large-firm practice by comparing its features with those of solo and small-firm practice. To do so, however, one must draw a somewhat arbitrary line between large and small firms. For present purposes, the key distinction is that most large firms, unlike their traditional counterparts, are bureaucracies.<sup>15</sup> Their structure encourages or requires the use of bureaucratic devices such as policy manuals, committees, specialized departments, management consultants and lay office managers, peer review and mentoring programs, loss-prevention protocols, centralized billing systems, and sophisticated computer programs for identifying conflicts of interest. For example, large firms are relatively likely to have multiple and far-flung branch offices, whose activities must be coordinated.<sup>16</sup> Because large firms recruit many lawyers laterally from other firms,<sup>17</sup> they cannot rely solely on their internal "culture" to ensure that all their lawyers behave properly. And because their associate-to-partner ratios can be as high as four-to-one, they need formal supervisory policies and routines.<sup>18</sup>

By our observation, at least some trappings of bureaucracy exist in most firms with more than ten lawyers. Accordingly, one may regard all such firms as "large," bearing in mind that they vary greatly in size and that the paradigmatic large firm for our purposes has many more than ten lawyers. Obviously, twelve-lawyer firms are more likely to function like eight-lawyer than hundred-lawyer firms, but the point remains that the larger the firm, the stronger the bureaucratic imperative.

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14. *Maturing Market Will Affect Profession in 90s*, B. LEADER, Sept.-Oct. 1990, at 11.

15. See ABEL, *supra* note 12, at 199 (stating that structural developments in large law firms "have increasingly compelled them to adopt the bureaucratic forms of their corporate clients"). However, some large firms strive to avoid bureaucracy. See, e.g., ROBERT L. NELSON, PARTNERS WITH POWER: THE SOCIAL TRANSFORMATION OF THE LARGE LAW FIRM 99-100, 107-14 (1988) (describing two large Chicago firms where the partners opted to trade off administrative efficiency in order to preserve their "baronial privileges" and independence).

16. By the mid-1980s, virtually all of the 100 largest firms in the country had branch offices. ABEL, *supra* note 12, at 59.

17. More than 25% of the 500 largest American law firms in 1987 recruited at least half of their partners from other firms. See Steve Nelson, *Lateral Hiring Established as Major Component of Recruiting Process*, OF COUNSEL, May 18, 1987, at 8. A recent study of the Illinois bar revealed that firms with fewer than twenty lawyers were much less likely than larger firms to hire laterally. SUSAN P. SHAPIRO, TANGLED LOYALTIES: CONFLICT OF INTEREST IN LEGAL PRACTICE 202 (2002).

18. ABEL, *supra* note 12, at 315. The mean and median number of associates per partner in New York City's ten largest law firms rose from .6 in 1950 to nearly 3 in 1985, *id.* at 314, but the trend has slowed and perhaps been reversed in recent years. On the impetus for high associate-to-partner ratios, see generally Galanter & Palay, *supra* note 13.

Large firms, so understood, differ from solo practices and small firms not only in their tendency to have multiple offices, recruit laterally, and maintain high associate-to-partner ratios, but also in their location, clientele, practice fields, and degree of lawyer specialization. All these features have potential regulatory implications.

First, large firms are concentrated in urban areas where the bar is neither small, nor tight-knit, nor particularly stable in composition.<sup>19</sup> Moreover, since many large firms have clients and offices in several states (or countries), their lawyers often practice across jurisdictional lines and interact only sporadically with lawyers and officials in any one locale. As a result, although large firms try to cultivate good *institutional* reputations in the regional, national, or international markets they serve, their lawyers' personal reputations may not be well known or crucial in any local legal community.

Second, large firms have a distinctive clientele. Solo practitioners and small firms tend to represent individuals. Their clients are often legally unsophisticated and face the sorts of legal problems that afflict ordinary people—e.g., divorce, DUI charges, personal bankruptcies, personal-injury and workers' compensation claims. By contrast, large firms generally represent entities—typically businesses, but non-profit associations and government units as well.<sup>20</sup> Entity clients are often managed by legally-sophisticated executives and may employ inside counsel who can monitor the performance of outside counsel.<sup>21</sup> Having recurring legal needs, entity clients are also relatively likely to have ongoing relationships with their lawyers.

Because disciplinary proceedings are rarely instituted unless a client files a grievance with bar authorities,<sup>22</sup> this difference in clientele goes a long way toward explaining why, even today, disciplinary targets are almost always solos

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19. See ABEL, *supra* note 12, at 180 (observing that the decline in the proportion of American lawyers in small firms is a concomitant of the shift in practice from rural to urban environments).

20. In the late 1960s, sole practitioners derived 65% of their receipts from individuals and only 20% from businesses, while firms with twenty to forty-nine lawyers derived only 6% of their receipts from individuals and 78% from businesses; this gulf widened in the 1970s. *Id.* at 202–03. The proportion of their fees that private practitioners earned from individual clients fell below 50% around 1980, *id.* at 203, and has continued to dwindle. This change correlates directly with the growth of large firms.

21. Roughly 10% of the lawyers practicing in the U.S. are employed as in-house counsel by business or non-profit organizations. CLARA N. CARSON, THE LAWYER STATISTICAL REPORT: THE U.S. LEGAL PROFESSION IN 1995, at 1, 7 (1999). Like lawyers in large firms, in-house counsel and government lawyers work in bureaucratic settings and are rarely the targets of state disciplinary proceedings.

22. The disciplinary process is reactive, not proactive. Rather than ferreting out misconduct on their own, disciplinary authorities typically wait for disgruntled clients to file grievances before investigating. See Eric H. Steele & Raymond T. Nimmer, *Lawyers, Clients, and Professional Regulation*, 1976 AM. B. FOUND. RES. J. 919, 922–23 (1976).



and small-firm lawyers.<sup>23</sup> A recent report by the California State Bar<sup>24</sup> makes the point:

[L]arge law firms generally represent large institutional or business clients who are often in a very powerful bargaining position and able to compel satisfactory performance from their lawyers. When their clients are dissatisfied, they can afford to change attorneys, negotiate for a reduction in fees, or litigate. They do not call upon the State Bar for assistance. On the other hand, clients of solo practitioners and small firms tend to be individuals with much less leverage in the attorney/client relationship, and hence these clients are more likely to bring their problems to the State Bar's attention.<sup>25</sup>

Third, although American lawyers of every stripe are more specialized than in the past, the trend is most pronounced in large firms.<sup>26</sup> By 1977, the proportion of lawyers nationwide who derived at least 25% of their income from one practice field was more than five times higher for lawyers in firms with annual

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23. Despite the explosion in large-firm practice since the 1970s, disciplinary proceedings against lawyers in large firms have remained rare. A study conducted in the 1980s found that more than 80% of the lawyers disciplined in California, Illinois, and the District of Columbia were solo practitioners and none practiced in a firm with more than seven lawyers, yet many large firms existed in those jurisdictions by then. *See* ABEL, *supra* note 12, at 145 (referring to the study); *see also* STATE BAR OF N. M. TASK FORCE ON MINORITIES IN THE LEGAL PROFESSION II, THE STATUS OF MINORITY ATTORNEYS IN NEW MEXICO—AN UPDATE 43 (2000), *reprinted in* 28TH NATIONAL CONFERENCE ON PROFESSIONAL RESPONSIBILITY 127 (Am. Bar Ass'n Ctr. for Prof'l Responsibility, Coursebook, 2002) (noting that 93% of the recent disciplinary proceedings in the state involved solos or lawyers practicing in very small firms).

24. STATE BAR OF CAL., INVESTIGATION AND PROSECUTION OF DISCIPLINARY COMPLAINTS AGAINST ATTORNEYS IN SOLO PRACTICE, SMALL SIZE LAW FIRMS AND LARGE SIZE LAW FIRMS (June 2001), *reprinted in* 28TH NATIONAL CONFERENCE ON PROFESSIONAL RESPONSIBILITY 105 (Am. Bar Ass'n Ctr. for Prof'l Responsibility, Coursebook, 2002).

25. *Id.* at 117. Similarly, scholars have long observed that "one-shot" clients, who are mostly individuals, are much more likely than "repeat" clients to use the disciplinary process as a means of controlling their relations with lawyers. *See, e.g.,* JOEL F. HANDLER, *THE LAWYER AND HIS COMMUNITY: THE PRACTICING BAR IN A MIDDLE-SIZED CITY* 83 (1967). In other words, repeat-player business clients do not view the disciplinary process as a significant means of governing their relations with large-firm lawyers. This is not to say that those lawyers engage in little or no misconduct. *See, e.g.,* William B. Glaberson et al., *A Question of Integrity at Blue-Chip Law Firms*, *BUS. WK.*, Apr. 7, 1986, at 76 (noting that large firms are frequently charged with wrongdoing in civil suits and other non-disciplinary proceedings). Another interpretation is that the victims of their misconduct are often third parties who have no more to gain from the disciplinary process than business clients do. *Cf.* Robert E. O'Malley, *Preventing Legal Malpractice in Large Law Firms*, 20 *U. TOL. L. REV.* 325, 328 (1989) (stating that the majority of serious civil suits filed against large law firms are initiated by third parties).

26. However, some small-firm "boutiques" specialize in a single field such as plaintiffs' personal injury work. Most large firms offer their clients a broad range of services, but their individual lawyers are highly specialized.

receipts of over a million dollars than for lawyers in very small firms, where most of the dwindling number of general practitioners worked.<sup>27</sup>

Specialists seeking practice guidance can often consult “best-practice” guidelines that are issued by specialty bars,<sup>28</sup> not just the less specific rules of professional conduct that are addressed to all lawyers and applied in disciplinary cases. Because they tend to handle high-stakes corporate matters, large-firm lawyers must take pains to limit their exposure to civil liability.<sup>29</sup> Guidelines tailored to a lawyer’s specialty can be very helpful here. Compliance with those guidelines can be strong evidence that a lawyer’s conduct met the prevailing standard of care in his or her field.<sup>30</sup>

In representing entity clients, lawyers in large firms specialize in business litigation, complex transactional work, or regulatory fields such as tax, securities, banking, or environmental law. Transactional lawyers, of course, are not subject to the direct controls judges use to regulate litigators. Tax, securities, banking, and environmental lawyers have reason to worry much more about incurring civil and criminal liability and about becoming targets of enforcement actions initiated by

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27. ABEL, *supra* note 12, at 202. Similarly, a survey of Chicago lawyers around 1980 found that the proportion doing virtually all their work in only one field was 4.5% for solo practitioners, but almost four times higher for lawyers in firms of fifty or more; solos, on the other hand, were over three times more likely than large firm lawyers to do significant amounts of work in five fields or more. *See id.* This is no accident. Lawyers in large firms are better-positioned to develop a specialty. If work in their field dries up, their incomes need not fall dramatically because their firms hedge against that risk by doing many other kinds of work. Small firms have less opportunity to diversify their practice. *See* Ronald J. Gilson & Robert H. Mnookin, *Sharing Among the Human Capitalists: An Economic Inquiry into the Corporate Law Firm and How Partners Split Profits*, 37 STAN. L. REV. 313, 327–29 (1985) (explaining how practice in a full-service law firm whose lawyers agree to invest in developing different specialties and to provide returns to those investments on a predetermined basis rather than on the basis of actual outcomes helps lawyers exploit gains from diversification).

28. *See* Judith Kilpatrick, *Specialty Lawyer Associations: Their Role in the Socialization Process*, 33 GONZ. L. REV. 501, 508 (1997–98) (estimating that over 1,000 specialty bar associations now exist and observing that the number has risen sharply in recent years). For an example of specialty guidelines of particular interest to large-firm lawyers, see ABA Bus. Law Section Comm. on Legal Opinions, *Third-Party Legal Opinion Report, Including the Legal Opinion Accord*, 47 BUS. LAW. 167 (1991) (attempting to standardize procedures and terms used in preparing third-party legal opinions for use in certain business transactions).

29. They are also relatively likely to have substantial liability insurance. *See* 4 RONALD E. MALLIN & JEFFREY M. SMITH, *LEGAL MALPRACTICE* § 33.4 (4th ed. 1996) (reporting that large-firm lawyers are more likely than others to be insured and to have high policy limits). Many malpractice insurers have loss-prevention counsel who encourage—sometimes prod—law firms to adopt internal controls to reduce liability risks. *See* SHAPIRO, *supra* note 17, at 38 (giving examples of ways in which malpractice insurers promote loss prevention efforts in large law firms). Insurers today are arguably among the most important external “regulators” of large-firm practice. *See generally* Anthony E. Davis, *Professional Liability Insurers as Regulators of Law Practice*, 65 FORDHAM L. REV. 209 (1996).

30. *Cf.* MODEL RULES OF PROF’L CONDUCT, Scope, paras. 5–6 (2001) [hereinafter MODEL RULES] (stating that the Model Rules are not designed as a basis for determining civil liability).

agencies such as the IRS and SEC<sup>31</sup> than about the slim prospect of being called to account in a state disciplinary proceeding.<sup>32</sup>

### **The Nature, Source, and Treatment of Ethical Problems in Solo and Small-Firm Practice**

The most frequent disciplinary charges are neglecting clients' matters, failing to communicate with clients, charging extortionate fees, mishandling client funds, and lying to clients (often in order to conceal neglect).<sup>33</sup> These problems are common in solo and small-firm practice, but rare in large firms. One reason for the discrepancy, mentioned earlier, is that the relatively sophisticated and resourceful entities that large firms represent, often on an ongoing basis, can monitor and motivate their lawyers better than individual clients can.<sup>34</sup> In our view, an equally important reason is that large-firm lawyers are enveloped in bureaucracy. Solos and small firms do not practice on a scale that makes it feasible to employ the corps of assistants, filing clerks, bookkeepers, and paralegals who support large-firm lawyers, or use the sophisticated control mechanisms by which large firms keep track of deadlines, client funds, billing records and accounts, and the status of their engagements.

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31. Unlike state disciplinary authorities, such agencies may sometimes proceed against law firms, not just individual lawyers, and encourage lawyers in their field to follow guidelines issued by specialty bar groups. *See, e.g.,* Order to Cease and Desist for Affirmative Relief from Kaye, Scholer, Fierman, Hays & Handler, para. 5 (Mar. 11, 1992), reprinted in *THE ATTORNEY-CLIENT RELATIONSHIP AFTER KAYE, SCHOLER 347, 352* (PLI Corp. Law & Practice, Course Handbook Series No. 779, 1992) (providing that in preparing certain legal opinions for banking clients, the law firm "shall comply with applicable professional standards . . . (the current standards applicable herein are set forth in the Third-Party Legal Opinion Report of the Business Law Section of the American Bar Association).").

32. *See, e.g.,* Ted Schneyer, *From Self-Regulation to Bar Corporatism: What the S&L Crisis Means for the Regulation of Lawyers*, 35 S. TEX. L. REV. 639, 640 (1994) (noting that "in contrast to the barrage of lawsuits and enforcement actions launched against S&L lawyers, nearly all has been quiet on the disciplinary front"); Steve France, *Can the Bar Regulate the Large Law Firms?*, LEGAL TIMES, Jan. 31, 1994, at 28 (criticizing the non-response of state disciplinary authorities to allegations in federal banking agencies' civil suits and administrative enforcement actions that lawyers for failed savings-and-loan institutions had behaved unethically).

33. *See, e.g.,* 2001 ATT'Y REGISTRATION & DISCIPLINARY COMM'N SUP. CT. ILL. 2001 ANN. REP. 7 (Apr. 30, 2002) (listing the most frequent sources of grievances). The same report indicates that the practice fields most likely to spawn grievances over the years have been criminal law, domestic relations, tort, and real estate. *Id.* Large-firm lawyers are relatively unlikely to practice in these fields.

34. One might infer that when large-firm lawyers are called to account for lies or negligent misrepresentations, it will often be for statements made not to clients, but to third parties in an effort to further clients' aims. Interestingly, as large-firm practice has become prominent, courts have increasingly permitted third-party tort claims against law firms for negligent misrepresentation, thereby abandoning the traditional privity requirement in negligence suits against lawyers. *See, e.g.,* *McCamish, Martin, Brown & Loeffler v. F.E. Appling Interests*, 991 S.W.2d 787, 791-95 (Tex. 1999) (confirming that such claims are now recognized in Texas).

When clients complain about neglect, lack of communication, extortionate fees, or mishandled funds, they generally file disciplinary grievances rather than civil suits, because their losses are too modest to justify the time or expense of a lawsuit. Indeed, it is fair to say that the chief role of the disciplinary process in the United States today is to protect vulnerable consumers from exploitation.<sup>35</sup>

### **The Nature and Source of Ethical Problems in Large Law Firms**

The characteristic ethical problems that arise in large firms have a different source and are treated differently than the problems just discussed. They stem from the fact that the balance of risks and rewards associated with a course of action can be very different for the large-firm lawyer(s) who would be taking that course than it is for others in the firm, or the firm as a whole. Such problems can create tensions, often deteriorating into conflict, within the firm. Since the tensions ordinarily become manifest within the firm before they become evident to others, they are usually recognized and resolved internally, without the involvement of regulators.

Many problems of this sort involve conflicts of interest.<sup>36</sup> For example, client *C* may ask partner *A* for representation in a matter in which *A* foresees that

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35. See David B. Wilkins, *Who Should Regulate Lawyers?*, 105 HARV. L. REV. 799, 874 (1992) (stating that "individual clients complaining about inattention, low-level negligence, overpayment, or conversion of trust funds will often be better served by the . . . flexible, informal, and relatively inexpensive procedures found in many disciplinary agencies than they would be by malpractice suits"). Even clients who suffer substantial losses as a result of misconduct by solo practitioners may decline to file suit, because those lawyers are less likely than lawyers in large firms to carry liability insurance or possess substantial personal assets. See MALLIN & SMITH, *supra* note 29, § 33.4 (showing that large-firm lawyers are more likely than others to be insured and have high policy limits); Theodore J. Schneyer, *Mandatory Malpractice Insurance for Lawyers in Wisconsin—And Elsewhere*, 1979 WIS. L. REV. 1019, 1034–35 (1979) (reporting on a Wisconsin study that found that 99% of the respondents from law firms with ten or more lawyers, but only 46% of the solo practitioners, were insured); see also ABEL, *supra* note 12, at 206–07 (documenting a strong correlation between lawyer income and firm size).

36. As a law firm grows and takes on more clients, the frequency with which it must confront conflicts issues can increase dramatically. Lloyd Cutler once estimated that when his Washington, D.C., law firm had only twenty lawyers, one of every twenty matters that new clients brought to the firm raised conflicts issues, but that the ratio swelled to one-in-three once the firm grew to over 100 lawyers. Lloyd N. Cutler, *The Role of the Private Law Firm*, 33 BUS. LAW. 1549, 1549 (1978). It follows that as a firm grows, its incentive to invest in conflict avoidance techniques increases as well. See SHAPIRO, *supra* note 17, at 320 (finding a "dramatic" correlation between the size of law firms and the extent of the precautions they take to avoid conflicts). Of course, any lawyer, whether in solo practice or in a firm, can be presented with, or become involved in, conflicting engagements. By citing *certain kinds* of conflicts as examples of the ethical problems that are distinctive to large firms, we do not mean to suggest that conflicts are rare in solo or small-firm practice. On the contrary, they are common. Small-town lawyers, for example, must often confront conflicts issues because local clients with potentially adverse interests have few local lawyers to choose from.

C's interests might be adverse to those of a client represented (in other matters) by partner B.<sup>37</sup> One might call the tensions that can arise in such cases "conflicts over conflicts."<sup>38</sup> To grasp the nature of these conflicts, consider the example.

In deciding whether to accept C's new engagement, the *firm* would want to weigh the opportunity for new revenue, the risk of ruffling client feathers, and the risk that *its* reputation and bottom line will suffer if a conflict materializes and a client is harmed.<sup>39</sup> But suppose that A works mostly on projects for C, and that A's income, job satisfaction, and status in the firm are linked to retaining C's business.<sup>40</sup> Rejecting the engagement could send C elsewhere, and not only for representation in the new matter. For A personally, this risk may be grave. For similar reasons, however, taking on the new matter might sour B's relationship with one of *her* best clients. If B gets wind of the proposed engagement, she may, for her own reasons, press the firm to reject it.

Large firms have effective, though not foolproof,<sup>41</sup> procedures for identifying and dealing with such issues. Once the potential conflict is identified, the affected clients can often be persuaded to consent to the new representation. In

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37. These situations raise ethical issues for firms, not just for lawyers individually, because the courts and bar have long considered it improper for a lawyer to accept an engagement that another lawyer in her firm would be unable to accept because of a conflict of interest. See, e.g., MODEL RULES, *supra* note 30, at R. 1.10 (providing that "[w]hile lawyers are associated in a firm, none of them shall knowingly represent a client when any one of them practicing alone would be barred from doing so" by certain other rules governing conflicts). Because it is now very common for lawyers to contemplate moving from one firm to another, this conflict imputation rule is under fire and new exceptions are developing. See RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 124(2) & cmt. d(i) (2000) [hereinafter RESTATEMENT] (relaxing the imputation rule in some cases in which one lawyer in a firm is barred from representing a client because she had represented an adverse party in a related matter at another firm).

38. In relatively small law firms, where institutional loyalties tend to be stronger, conflicts over conflicts are relatively unlikely to arise. And the conflicts-of-interest issues that do arise are relatively easy to identify and can be resolved by one lawyer walking down the hall to another lawyer's office for a quick conference. In much larger firms, potentially conflicting engagements may involve not just two lawyers, but two departments, branch offices, or teams of lawyers.

39. *Ex ante*, it is often unclear whether or under what circumstances a firm may ethically accept such an engagement. For instance, lawyers may not represent a client when the representation will be "directly" adverse to another current client, unless the lawyers "reasonably" believe the engagement will not "adversely affect the relationship" with the other client and each client consents after adequate "consultation." MODEL RULES, *supra* note 30, at R. 1.7(a). The quoted terms are fraught with ambiguity. Moreover, if the firm accepts the engagement but is found *ex post* to have violated the rule by doing so, serious legal consequences may follow, including disqualification (if the engagement involves litigation), fee forfeiture, and civil liability for malpractice or breach of fiduciary duty. See RESTATEMENT, *supra* note 37, § 121 cmt. f (listing sanctions and remedies for conflicts).

40. With partners today often changing firms and with many business clients being more interested in specific lawyers than in their law firms, A may regard his best clients not only as a source of status at his current firm, but as his own portable assets!

41. See SHAPIRO, *supra* note 17, at 338-47 (providing empirical evidence that even the most sophisticated conflict-avoidance systems fail at times, and explaining how they fail).

some cases, engagements can be reframed to avoid the conflict. In others, the firm—acting through a managing partner, a committee, or some other centralized decisionmaker—may decide to accept the engagement without disclosing the potential conflict to *B*'s client or, for that matter, to either client. In that event, the firm is betting that a conflict will not materialize, or will not be detected outside the firm, or if detected will not be protested, or if protested will be resolved by “bulling it through.” If the gamble pays off, any misconduct that occurs<sup>42</sup> will remain invisible outside the firm.

Alternatively, *A* may try to circumvent his firm's procedures. Acting as the proverbial “rogue” lawyer, he might keep the conflict issue under wraps, hoping that it will stay under the firm's conflicts-checking radar. He might unilaterally decide that the potential conflict is so unlikely to materialize that the new matter can properly be accepted without eliciting the informed consent of both clients, or that the risks of accepting the matter without disclosure and consent are, in any event, worth running. From the firm's standpoint, *A* is badly situated to decide such things. Compared to his partners, *A* stands to gain disproportionately if the engagement is accepted. But his share of any losses the firm sustains if the risks materialize will generally be no greater than other partners' shares. And the larger the firm, the more partners *A* will have and the smaller his personal loss will be. Thus, the challenge for the firm is to develop internal controls that prevent individual opportunism such as *A*'s, or at least detect it in time to minimize the fallout for the firm.<sup>43</sup>

Finally, whether the engagement is accepted or not, one partner, *A* or *B*, may consider his or her practice to have been unduly constrained and leave the firm.<sup>44</sup> In extreme cases, a conflict over conflicts can lead to the dissolution of a firm and litigation between the partners.

Again, conflict-of-interest issues merely illustrate the distinctive source of ethical problems for large firms—namely, discrepancies between risk/reward balances for a particular lawyer, team, or department, and for the firm as a whole.

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42. Misconduct will have occurred, for example, if the firm had a duty to disclose the conflict issue to both clients and elicit their consent before proceeding, but failed to do so.

43. This hypothetical shows why it is so important for large firms not to permit a lawyer whose practice is directly affected to unilaterally resolve a conflict issue. For a discussion of large-firm deliberations regarding conflicts and other ethical issues, see EMMANUEL LAZEGA, *THE COLLEGIAL PHENOMENON: THE SOCIAL MECHANISMS OF CO-OPERATION AMONG PEERS IN A CORPORATE LAW PARTNERSHIP* (2001). It may make sense for small firms to allow individual lawyers to decide how to handle some conflict issues that arise in their own practices, but it is crucial for larger firms to channel such issues to disinterested decision-makers. Data suggest that virtually all large firms try to do so. See SHAPIRO, *supra* note 17, at 308, 318–19 (showing that virtually all large firms in Illinois uniformly have a policy against leaving the identification and resolution of conflicts issues to the lawyers directly involved). In Shapiro's study, the median size of the Illinois law firms that appoint disinterested “specialists” to review conflicts issues is 287 lawyers; the median size of firms that do not do so is sixteen lawyers). *Id.* at 319. Large firms that do not appoint conflicts or ethics “specialists” still expect conflict issues to be taken to a managing partner or management committee.

44. See *id.* at 200 (citing examples).

Economists use the term “tragedy of the commons” to refer to such problems.<sup>45</sup> A firm’s reputation and other assets constitute a “commons” for the lawyers who practice there.

All practitioners run some risks that their actions will later be found to have violated ethics rules or other laws governing lawyers. Litigators run the risk of violating discovery rules or the rule against filing frivolous pleadings or motions. Lawyers engaged in “office practice” run the risk of making actionable misrepresentations in regulatory filings, in the “representations and warranties” drafted for inclusion in a merger or acquisition agreement, or in legal opinions written on behalf of clients for use by third parties. Such risks go hand-in-hand with opportunities for reward. There are fees to be earned, clients to be satisfied, professional goals to be achieved, personal reputations to be enhanced. Walking close to the edge of ethical and legal propriety often promises the greatest rewards, just as it poses the greatest risks.

In solo practice, the risk/reward balance for lawyer and “firm” is the same, but in large firms institutional interests can diverge sharply from those of an individual lawyer, especially if her compensation is directly linked to her willingness to engage in risky conduct. In that case, the lawyer will benefit disproportionately if all goes well, but the legal and reputation costs that will accrue if a risk materializes will be spread throughout the firm. If the lawyer engages in wrongdoing that results in liability to a third party,<sup>46</sup> her firm and partners are likely to bear the brunt of any civil liability,<sup>47</sup> increased insurance expense, or reputational damage that ensues.<sup>48</sup>

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45 See Garrett Hardin, *The Tragedy of the Commons*, 162 SCIENCE 1244 (1968). The term refers to problems that can arise when a town maintains a public “commons.” The commons will be most valuable to the townspeople in the aggregate if no one misuses it. But individuals will be tempted to misuse the commons in hopes of reaping a substantial personal benefit while bearing only a small share of the resulting loss of value. *Id.*

46. Some scholars argue that large firms are better positioned than small firms to rebuff client pressure to engage in misconduct that furthers client interests at the expense of third parties. Professor Ribstein, for example, claims that the size and diversity of a large firm’s client base “cushion[s] the financial shock of losing a big client.” Larry E. Ribstein, *Ethical Rules, Agency Costs, and Law Firm Structure*, 84 VA. L. REV. 1707, 1740 (1998). This supposedly allows the firm to credibly threaten to “fire” such clients and, more generally, to serve as a “buffer between the illegitimate desires of . . . clients and the social interest.” ERWIN SMIGEL, *THE WALL STREET LAWYER: PROFESSIONAL ORGANIZATIONAL MAN?* 335 (1969). The analysis presented in this Article throws the validity of this argument into doubt. See also Ted Schneyer, *Reputational Bonding, Ethics Rules, and Law Firm Structure: The Economist as Storyteller*, 84 VA. L. REV. 1777, 1787–90 (1998) (criticizing the same argument). If decisions are made by the partner in charge of a matter, the *relevant* client base may be that partner’s, not the firm’s. And the partner’s client base may be quite narrow. See NELSON, *supra* note 15, at 250 (providing evidence that corporate lawyers in large firms on average devote almost half their time to their biggest client’s matters).

47. Firms are vicariously liable for their lawyers’ work-related torts. In general partnerships, partners who were uninvolved in tortious conduct are also vicariously liable. In recent years, of course, many firms have become limited liability entities. See, e.g., Charles W. Wolfram, *Inherent Powers in the Crucible of Lawyer Self-Protection: Reflections on the LLP Campaign*, 39 S. TEX. L. REV. 359, 360–61 & n.6 (1998). But even

Of course, firms can reduce some discrepancies between individual and collective interests by not compensating lawyers directly for the revenue they generate. But many firms feel compelled to use that compensation system, lest their lawyers become unproductive or bolt to firms that do use it. Other techniques can also help to align individual and collective interests.<sup>49</sup> Moreover, although lawyers in small firms are more apt to create strong personal ties, even large firms can cultivate institutional loyalty. Still, the “distance” between lawyer and firm interests tends to vary directly with firm size.

### The Treatment of Ethical Problems in Large Firms

Large-firm engagements involve not only sophisticated clients, but high stakes and intricate legal problems. In addition, they are often assigned to teams rather than to an individual lawyer. Other things being equal, the higher the client’s stake, the greater the risk to the firm. The more intricate the problem, the greater the risk of botching it. And the larger the team, the greater the risk of a breakdown in communication and coordination. Elaborate internal controls notwithstanding, things can and do go wrong. What happens then?

If a client (or an adversely affected third party) objects to a firm’s handling of an engagement, it will lodge its objection with the firm’s management. If management agrees with the objection, the matter will be resolved quietly. The firm may withdraw, help the client find another firm, forgo its fee, or compensate the client for its losses. The client will be more or less satisfied and it will be tacitly understood that no disciplinary grievance will be filed.

If management considers the objection unfounded, or simply refuses to acknowledge that misconduct occurred, the firm will gird itself for what may be a long and expensive battle. Typically, the client initiates the battle by filing a civil

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in those firms, a wrongdoing lawyer’s superiors may be personally liable for negligent supervision. *Id.* at 386–88. See also *FDIC v. Nathan*, 804 F. Supp. 888, 897–98 (S.D. Tex. 1992) (rejecting a law-firm principal’s argument that he could not be personally liable for negligent transactional work he did not perform, because he allegedly was responsible for supervising those who did the work).

48. For an argument that the larger the firm, the greater the institutional reputation it must protect against adverse publicity and, therefore, the stronger its motivation to deter internal wrongdoing, see Ribstein, *supra* note 46, at 1715–16. We concede that large firms have substantial reputations to protect and that those reputations can be damaged by adverse publicity. But we disagree with Ribstein’s implication that large firms can be regulated by means of “reputational bonding” even in the absence of serious liability risks. In our view, lawsuits are a key source of adverse publicity, so that the efficacy of reputational bonding as a control on large firms depends on the scope of their potential liabilities under existing law.

49. For example, Baker & McKenzie, a law firm with offices around the world, not only makes it a policy to strip a billing partner of credit for fees that are charged to a client before the firm’s director of professional responsibility has “signed off” on a relevant conflicts issue, but has a procedure (unused as of early 2002) to allocate the firm’s costs to a specific lawyer or branch office whose intentional violation of firm rules causes a problem for the firm. See *Conference Panelists Offer Insights on Managing Risks in Law Practice*, 70 No. 38 U.S.L.W. 2631, 2632 (Apr. 9, 2002).



suit, perhaps accompanied by a disciplinary grievance. If a grievance is filed, however, disciplinary proceedings will normally be stayed pending resolution of the civil suit, at which time it will be abandoned. By pursuing the civil suit, the client may recover a substantial amount of money from the firm's malpractice carrier and/or the firm itself. Pursuing a grievance yields no comparable benefits.<sup>50</sup>

To be sure, disciplinary agencies are authorized to open investigations and file disciplinary charges *sua sponte*. But they are chronically strapped for resources and unenthusiastic about proceeding against resourceful large-firm lawyers. Moreover, proving which lawyer(s) in a large firm committed a disciplinable offense can be difficult because those lawyers typically work in teams.<sup>51</sup> And most disciplinary agencies have no jurisdiction over law firms as such.<sup>52</sup>

In sum, large firms are often sued, and not infrequently disqualified from litigation on conflict-of-interest grounds. But their lawyers are seldom respondents in disciplinary proceedings. Thus, a key issue in regulating large-firm practice is whether existing civil remedies are adequate.

### A Transnational Perspective

The available literature suggests that our analysis applies not only in the United States, but also in other countries with modern legal professions.<sup>53</sup> The disciplinary process in those countries is no more active than in the United States, and is typically less so.<sup>54</sup> But even where discipline effectively regulates solos and small-firm lawyers, the universal prospect is that it will be of little significance in

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50. See Schneyer, *supra* note 32, at 645–46 (noting that although disciplinary agencies sometimes order restitution of client funds and property, they do not make damage awards and most do not use fines as sanctions).

51. See Ted Schneyer, *Professional Discipline for Law Firms?*, 77 CORNELL L. REV. 1, 8–11 (1991) (discussing the importance of teams in large-firm practice and explaining how teaming complicates disciplinary enforcement).

52. But see N.J. SUP. CT. R. 1:20-1 (amended July 10, 1998) (asserting disciplinary jurisdiction over every “business entity” authorized to practice law in the state); *In re Ravich, Koster, Tobin, Oleckna, Reitman & Greemstein*, 715 A.2d 216, 221–22 (N.J. 1998) (reprimanding law firm after partners agreed that the firm would solicit clients in-person at a mass disaster site); *New York Adopts New Rules Subjecting Firms to Discipline*, 12 Laws. Man. On Prof. Conduct (ABA/BNAL) 191, 191 (June 12, 1996) (noting new provisions of New York’s Code of Professional Responsibility that are addressed to, and enforceable against, law firms).

53. On professional regulation in England, see generally ANDREW BOON & JENNIFER LEVIN, *THE ETHICS AND CONDUCT OF LAWYERS IN ENGLAND AND WALES* (1999); MARY SENEVIRATNE, *THE LEGAL PROFESSION: REGULATION AND THE CONSUMER* (1999). On Canada, see HURLBURT, *supra* note 8; ALLAN C. HUTCHINSON, *LEGAL ETHICS AND PROFESSIONAL RESPONSIBILITY* (1999). On France, see LEUBSDORF, *supra* note 8. On Australia, see STAN ROSS, *ETHICS IN LAW: LAWYERS’ RESPONSIBILITY AND ACCOUNTABILITY IN AUSTRALIA* (2d ed. 1998).

54. Many countries have ethical codes for lawyers. By all accounts, however, including those cited in the previous footnote, their disciplinary systems are weak and rarely utilized.

governing professional conduct in large firms.<sup>55</sup> Clients of large firms will instead depend heavily on the self-interest of those firms, particularly their interest in maintaining good reputations with the CEOs, CFOs, and general counsel of the large companies that buy legal services in regional, national, and international markets. To protect their interests, large firms will continue to develop internal controls to curb misconduct that stems from individual-lawyer opportunism. They will also be responsive to complaints from clients (or third parties) that they find justified or worrisome. Whether they consider a complaint worrisome, however, will depend on the scope of the civil remedies that are available—i.e., on the “law of lawyering” as distinct from legal ethics. In most countries, that law remains to be developed.

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55. See Richard L. Abel, *The Future of the Legal Profession: Transnational Law Practice*, 44 CASE W. RES. L. REV. 737 (1994); Mary C. Daly, *The Ethical Implications of the Globalization of the Legal Profession*, 21 FORDHAM INT'L L.J. 1239 (1998).